

**FORM 10-K**  
**SECURITIES AND EXCHANGE COMMISSION**  
**WASHINGTON, D.C. 20549**

(X) ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)  
OF THE SECURITIES EXCHANGE ACT OF 1934 (FEE REQUIRED)

For the fiscal year ended December 31, 1999

( ) TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934 (NO FEE REQUIRED)

Commission File No. 0-22825  
**RCN CORPORATION**

(Exact name of registrant as specified in its charter)

Delaware	22-3498533
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

105 Carnegie Center, Princeton, New Jersey	08540
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number including area code: 609-734-3700  
Securities registered pursuant to Section 12(b) of the Act: None  
Securities registered pursuant to Section 12(g) of the Act:

Common Stock, par value \$1.00 per share  
(Title of Class)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

X Yes    No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. (X)

Number of shares of the Registrant's Stock (\$1.00 par value) outstanding at February 29, 2000

78,114,901 Common Stock

Aggregate market value of Registrant's voting stock held by non-affiliates at February 29, 2000 computed by reference to closing price as reported by NASDAQ for Common Stock (\$59.88 per share)

\$2,811,922,404 Common Stock

Documents Incorporated by Reference

I. Proxy Statement for 2000 Annual Meeting of Shareholders is incorporated by reference into Part I and Part III of this Form 10-K.

**OFFICIAL FILE**

Pet I.C.C. DOCKET NO. 00-060K  
Pet KRC Exhibit No. Pet 4X A C  
Witness \_\_\_\_\_  
Date \_\_\_\_\_ Reporter \_\_\_\_\_

## PART I

Some of the statements made by RCN in this 10-K are forward looking in nature. Actual results may differ materially from those projected in forward-looking statements as a result of a number of factors. We believe that the primary factors include, but are not limited to uncertainties relating to economic conditions, acquisitions and divestitures, government and regulatory policies, the pricing and availability of equipment, materials, inventory and programming, our ability to develop and penetrate existing and new markets, technological developments and changes in the competitive environment in which we operate. Additional information concerning these and other important factors can be found in our filings with the Securities and Exchange Commission. Statements in this release should be evaluated in light of these important factors.

### Item 1. BUSINESS

#### Overview

We are the nation's first and largest single-source facilities-based provider of bundled local and long distance phone, cable television and high-speed Internet services to the densest residential markets in the country. We are currently delivering broadband services over our Megaband(tm) Network and designing and building our network on both the East and West coasts as well as in Chicago. In addition, we are a leading Internet Service Provider ("ISP") in our markets. We offer individual or bundled service options, superior customer service and competitive prices. We are also constructing our networks with significant excess capacity in order to accommodate expanded services in the future. We intend to expand the services provided to our customers through strategic alliances and opportunistic development of complementary products. In addition, we intend to use the excess capacity in our fiber optic networks to provide services to commercial customers located on or near our networks.

Our Megaband(tm) Network is a unique broadband fiber-optic platform capable of offering a full suite of communications services including fully featured voice, video and high-speed Internet to residential customers. The network employs SONET ring backbone architecture, and localized nodes built to ensure that our state-of-the-art fiber optics travel to within 900 feet of our customers, with fewer electronics and lower maintenance costs than existing local networks. Our high-capacity local fiber-optic networks target densely populated areas comprising 44% of the US residential communications market spread over just 6% of its geography. Additional information can be found at [www.RCN.com](http://www.RCN.com).

Our initial fiber optic networks have been established in selected markets in the Boston to Washington, D.C. corridor, including New York City, and also in the San Francisco Bay area. In addition, we have recently entered into agreements that will allow us to establish and expand our advanced fiber optic networks in the Los Angeles and Chicago areas. We are typically building the first true local network to compete with the aging infrastructure of the incumbent service providers in our markets. In the Boston market we operate our advanced fiber optic network through a joint venture with NSTAR Communications, Inc. or "NSTAR" or "Boston Edison Company" or "BECO". Currently, we own 76.86% interest in and manage the joint venture. Prior to the close of business on December 31, 1999, we owned 53.88%. The joint venture is accounted for on a consolidated basis. In the Washington, D.C. market, we are developing an advanced fiber optic network through a joint venture named Starpower with Pepco Communications, L.L.C. ("PEPCO") an indirect wholly owned subsidiary of Potomac Electric Power Company. We own 50% of Starpower and Pepco Communications owns 50% and it is accounted for under the equity method of accounting. We believe that these joint ventures provide us with a number of important advantages. For example, we are able to access rights-of-way of our joint venture partners and use their existing fiber optic facilities. This allows us to enter our target markets quickly and efficiently and to reduce the up-front costs of developing our networks. In addition, our joint venture partners provide us with access to additional assets, equity capital and established customer bases.

We also benefit from our relationship with our largest shareholder, Level 3 Communications, Inc., and from the experience gained by certain of our key employees who participated in the operation and development of other telephone, cable television and business ventures, including MFS Communications Company, Inc.

Because we deliver a variety of services, we report the total number of our various service connections purchased for local telephone, video programming and Internet access rather than the number of customers. For example, a single customer who purchases local telephone, video programming and Internet access counts as three connections. Since we view long distance as a complementary product we do not currently include customers of our long distance as connections. See "Connections." As of December 31, 1999, we had approximately 947,000 connections which were delivered through a variety of our owned and leased facilities including hybrid fiber/coaxial cable systems, a wireless video system and advanced fiber optic networks. As of that date, we had approximately 223,000 total connections attributable to customers connected to advanced fiber optic networks ("on-net" connections) and had approximately 724,000 connections attributable to customers served through other facilities ("off-net" connections).

We have extensive operating experience in both the telephone and video industries and in the design, development and construction of telecommunications facilities. Our experience provides us with expertise in systems operation and development, and gives us an established infrastructure for customer service and billing for both voice and video services and established relationships with suppliers of equipment and video programming. In addition, our management team and board of directors benefit from experience gained when they managed C-TEC Corporation ("C-TEC"), which, prior to September 30, 1997, owned and operated our company. C-TEC has over 100 years of experience in the telephone business and nearly 25 years of experience in the cable television business. Both C-TEC and certain members of management also have extensive experience in the design and development of advanced telecommunications facilities.

We seek to exploit competitive opportunities in selected markets where population density, favorable demographics and the aging infrastructure of the incumbent service providers' network facilities combine to create a particularly attractive opportunity to develop advanced fiber optic networks. We continue to construct network facilities within the Boston- to-Washington, D.C. corridor. We believe that our experience in the Northeast will provide us with a key strategic advantage as we enter markets in the San Francisco-to-San Diego corridor and in Chicago.

#### Business Strategy

Our goal is to become the leading provider of communications services to residential customers in our target markets by pursuing the following key strategies:

**Exploit the "Last Mile" Bottleneck in Existing Local Networks:** Existing local networks are typically low capacity, single service facilities without the bandwidth for multiple or new services and revenue streams. Investment in the local network or "last mile" has not generally kept pace with other industry and technological advances. In our target markets, we seek to be the first operator of an advanced fiber optic network offering advanced communications services to residential customers.

**Continue Construction of Advanced Fiber Optic Networks:** Our advanced fiber optic networks are designed with sufficient capacity to meet the growing demand for high speed, high capacity, voice, video and data services. Our networks also have a significant amount of excess capacity at relatively low incremental cost which will be available for the introduction of new products. We believe that our high capacity advanced fiber optic networks provide us with certain competitive advantages such as the ability to offer bundled services and the opportunity to recover the cost of our network through multiple revenue streams. In addition, our networks generally provide superior signal quality and network reliability relative to the typical networks of the incumbent service providers.

**Leverage our Network and Customer Base:** We are able to leverage our network by delivering a broad range of communications products and by focusing on high density residential markets. This bandwidth capacity and home density allows us to maximize the revenue potential per mile of constructed network. We believe we can further exploit our network capacity and customer base by exploring opportunities to deliver new products and services in the future, including complementary commercial and wholesale products and services.

**Offer Bundled Voice, Video and Data Services with Quality Customer Service:** We offer our customers a single-source package of competitively priced voice, video and data services, individually or on a bundled basis, with quality customer service. By connecting customers to our own network, we improve our operating economics and have complete control over our customers' experience with us. We believe that the combination of bundled communications services and quality customer care that we provide is superior to services that are typically available from most incumbent telephone, cable or other service providers.

**Continue to Use Strategic Alliances:** We have been able to enter markets quickly and efficiently and to reduce the up-front capital investment required to deploy our networks by entering into strategic alliances with companies such as Boston Edison Company, Pepco Communications, Level 3, Qwest, MCI/WorldCom and Southern California Edison. By establishing relationships with these companies, we are able to take advantage of their existing extensive fiber optic networks and other assets, and our own existing cable television infrastructure, to expedite and reduce the cost of market entry and business development. We will continue to evaluate other strategic alliances in our existing markets and our developing markets.

#### **Network Development and Financing Plan**

Because our network development plan involves relatively low fixed costs, we are able to schedule capital expenditures to meet expected subscriber growth in each major market. *Our principal fixed costs in each such market are incurred in connection with the establishment of a video transmission and telephone switching facility.* To make each market economically viable, it is then necessary to construct infrastructure to connect a minimum number of subscribers to the transmission and switching facility. We phase our market entry projects to ensure that we have sufficient cash on hand to fund this construction.

Based on our current growth plan, we expect that we will require a substantial amount of capital to expand the development of our network and operations into new areas within our larger target markets. We need capital to fund the construction of our advanced fiber optic networks, upgrade our hybrid fiber/coaxial plant and fund operating losses and repay our debts. We currently estimate that our capital requirements for the period from January 1, 2000 through 2001 will be approximately \$3.6 billion, which include capital expenditures of approximately \$1.4 billion in 2000 and approximately \$1.6 billion in 2001. These capital expenditures will be used principally to fund additional construction of our fiber optic network in high density areas in the Boston, New York City, Washington, D.C. and San Francisco Bay area markets as well as to expand into new markets (including selected markets in the western United States) and to develop our information technology systems. These estimates are forward-looking statements that may change if circumstances related to construction, timing of receipt of regulatory approvals and opportunities to accelerate the deployment of our networks do not occur as we expect. In addition to our own capital requirements, our joint venture partners are expected to contribute approximately \$350 million, of which approximately \$265 million has been contributed, to the joint ventures through 2001 in connection with development of the Boston and Washington, D.C. markets.

In order to facilitate growth beyond 2000, we expect to supplement our existing available credit facilities and operating cash flow by continuing to seek to raise additional capital to increase our network coverage and pay for other capital expenditures, working capital, debt service requirements and anticipated further operating losses. We may seek sources of funding from vendor financing, public offerings or private placements of equity and/or debt securities, and bank loans.

#### RCN Services

We provide a wide range of local and long distance telephone, video programming and data services, both individually and in bundled service options.

We provide these services through a range of facilities including our advanced fiber optic networks in New York City, Boston and Washington D.C. areas, California, a wireless video system in the New York City, our hybrid fiber/coaxial cable systems in the states of New York (outside New York City), New Jersey and Pennsylvania. We also provide, on a limited basis, resale local and long distance telephony services.

Connections. The following table summarizes the development of our subscriber base:

	As of				
	<u>12/31/98</u>	<u>3/31/99</u>	<u>6/30/99</u>	<u>9/30/99</u>	<u>12/31/99</u>
On-Net Service Connections:					
Voice .....	30,868	40,215	49,539	56,209	62,733
Video .....	86,349	99,098	110,565	120,353	138,577
Data .....	<u>6,167</u>	<u>9,922</u>	<u>13,024</u>	<u>17,985</u>	<u>21,654</u>
Subtotal On-Net.....	<u>123,393</u>	<u>149,235</u>	<u>173,128</u>	<u>194,547</u>	<u>222,964</u>
Off-Net:					
Voice .....	65,022	60,004	54,917	49,271	46,986
Video .....	175,313	170,323	165,523	164,859	153,627
Data .....	<u>491,633</u>	<u>506,180</u>	<u>508,992</u>	<u>535,107</u>	<u>523,728</u>
Subtotal Off-Net.....	<u>731,968</u>	<u>736,507</u>	<u>729,432</u>	<u>749,237</u>	<u>724,341</u>
Total Service Connections.....	<u>855,361</u>	<u>885,742</u>	<u>902,560</u>	<u>943,784</u>	<u>947,305</u>
Homes Passed.....	304,505	350,733	427,843	550,771	713,823
Marketable Homes.....	270,406	301,546	361,015	440,112	551,006

Because we deliver a variety of services to our customers, we quantify our customer activity by the number of individual local telephone, video programming or Internet access services, or "connections", purchased. Consequently, a single customer purchasing local telephone, video programming and Internet access counts as three connections.

We classify connections in the "Off-Net" category until the relevant facilities are capable of providing voice, video and data services, including local telephone service, through an RCN switch.

"Off-Net-Voice" figures in the table above represent resold local phone service provided to customers not connected to the advanced fiber optic networks.

"Off-Net-Video" figures in the table above include at December 31, 1999 approximately 32,000 wireless connections and approximately 4,000 wireline video connections serving the University of Delaware.

As of December 31, 1999 we had approximately 135,000 homes passed and approximately 122,000 basic subscribers connected to our hybrid fiber/coaxial cable system in the New York, New Jersey and Lehigh Valley service areas.

In areas served by our joint ventures in the Greater Boston and Washington, D.C. areas, the subscribers are customers of the relevant joint venture and are fully included in the connections reflected in the table above.

We report marketable homes, which represent that segment of homes passed to which are marketing our entire line of advanced fiber optic network products. The distinction between homes passed and marketable homes recognizes our transition from constructing our network in initial markets to providing services to customers that have ordered our services.

Set forth below is a brief description of our services:

**Voice.** We offer full-featured local exchange telephone service, including standard dial tone access, enhanced 911 access, operator services and directory assistance. We compete with the incumbent local exchange providers and competitive local exchange carriers ("CLECs"). In addition, we offer a wide range of value-added-vertical services, including call forwarding, call waiting, conference calling, speed dial, calling card, 800-numbers and voice mail. We also provide Centrex service and associated features. Our local telephone rates are generally competitive with the rates charged by the incumbent providers. At December 31, 1999, we had approximately 63,000 telephone service connections on our advanced fiber optic networks and approximately 47,000 customers for resold telephone service. We also provide competitively priced long distance telephone services, including outbound, inbound, calling card and operator services. These services are offered to residential and business customers.

**Video Services.** We offer a diverse line-up of high quality basic, premium and pay-per-view video programming. Depending on the system, we offer from 60 to 150 channels. Our basic video programming package provides extensive channel selection featuring all major cable and broadcast networks. Our premium services include HBO, Cinemax, Showtime and The Movie Channel, as well as supplementary channels such as HBO Plus, HBO Signature and Moremax. In Demand PPV, available on our advanced fiber optic networks, uses the latest "impulse" technology allowing convenient impulse pay-per-view ordering of the latest hit movies and special events instantly from the customer's remote. "Music Choice" offers 31-45 different commercial-free music channels delivered to the customer's stereo in digital CD quality sound.

As of December 31, 1999, we had approximately 139,000 subscribers for our video programming services provided over advanced fiber optic networks. As of such date, we also had approximately 32,000 connections attributable to the wireless video system and approximately 122,000 connections attributable to the hybrid fiber/coaxial cable systems.

**Internet Access and Data Transmission.** We operate as an Internet service provider under the RCN.com brand name. We focus on serving individuals and businesses through a network of our owned points of presence ("POPs") which are connected to our advanced fiber optic network. Our primary service offerings are 56K dial-up and high-speed cable modem access. We also sell commercially oriented private line point-to-point data transmission services such as DS-1 and OC-3 and a range of web page and server hosting services. Our subscribers use their RCN accounts to communicate, retrieve and publish information on the Internet. We believe that we are the largest regional provider of Internet services in the Northeast United States. As of December 31, 1999, we had approximately 545,000 Internet subscribers.

### Migration of Customers to Advanced Fiber Networks

We provide wireless video services to customers located near our advanced fiber optic network in New York City and dial-up Internet services to acquired subscribers. We have also actively marketed resold telephone service in the past. Our goal is to extend our advanced fiber optic network to service many of those customers. As our advanced fiber optic network is extended into these areas or buildings, customers receiving wireless video service in New York City are switched to the advanced fiber optic network from the wireless video network. The wireless video equipment is then used to provide services to other customers in off-network premises. Similarly, as the advanced fiber optic network is developed, voice and data customers are switched to the advanced fiber optic network from resale and dial-up accounts. The switch to our network allows us to gain additional revenue and higher margins from originating and terminating access fees and to control the related services and service quality.

### Strategic Relationships and Facilities Agreements

We have entered into a number of strategic alliances and relationships which allow us to penetrate the telecommunications services market early and to reduce the cost of entry into our markets. We expect to continue to pursue potential opportunities from entering into strategic alliances to facilitate network expansion and entry into new markets.

### Southern California Edison

We have an agreement with Southern California Edison ("SCE") that will help us utilize SCE's existing fiber backbone and construction expertise to expedite our entry and expansion into the greater Los Angeles area. The agreement will enable us to reach 1.5 million households in an area with a density of more than 200 homes-per-mile of plant.

The general agreement calls for SCE to install communications cable for us in areas where we secure municipal franchises. In addition, Edison Carrier Solutions, SCE's division that provides wholesale telecommunications services, will provide transport for our telecommunications traffic over the Edison Carrier Solutions' high-speed network.

### BECO Joint Venture

In 1996 RCN and the Boston Edison Company, through wholly-owned subsidiaries, formed a joint venture to use 126 fiber miles of BECO's fiber optic network to deliver our comprehensive communications package in Greater Boston. A joint venture agreement provided for the organization and operation of RCN-BECOCOM, LLC, an unregulated entity with a term expiring in the year 2060. RCN-BECOCOM is a Massachusetts limited liability company organized to own and operate an advanced fiber optic telecommunications network and to provide, in the market in and around Boston, Massachusetts, voice, video and data services. Prior to the close of business at December 31, 1999 we owned 53.88% of the equity interest in RCN-BECOCOM and BECO owned the remaining 46.12% interest. This joint venture with BECO is reflected in our financial statements on a consolidated basis.

Pursuant to an exchange agreement between BECO and RCN, BECO has the right, from time to time, to convert portions of its ownership interest in RCN-BECOCOM into shares of our common stock, based on an appraised value of such interest. Shares issued upon such exchanges are issued to NSTAR Communications Securities Corporation ("NSTAR Securities"). In 1999, BECO and the Company entered into two exchange transactions pursuant to which BECO converted a portion of its ownership interest into RCN common stock which was issued to NSTAR Securities. Prior to such exchange transactions, BECO owned a 49% interest in the joint venture. On February 19, 1999, BECO exchanged a portion of its interest for 1,107,539 shares of RCN common stock. Such portion of the interest was valued as of January 15, 1998. On December 31, 1999, BECO exchanged a further portion of its interest for 2,989,543 shares of RCN common stock. Such portion of the interest was valued as of May 27, 1999. Following such exchanges, BECO retains a 23.14% sharing ratio in the joint venture, and the right to invest as if it owned a 49% interest. Such investment percentage will decrease to the extent NSTAR Securities disposes of such RCN common stock.

We expect to benefit from our ability to use BECO's large fiber optic network, its focus on innovative technology, its sales and marketing expertise and its reach into the Boston market. In the future, the venture may expand into energy management and property monitoring services. Starting in Boston, the joint venture partners have expanded into surrounding markets, including the cities of Arlington, Somerville and Newton, Massachusetts. As a result of our access to the extensive BECO network, our reliance on and use of MFS/WorldCom facilities in Boston has been reduced significantly.

#### *Starpower Joint Venture*

In 1997, RCN Telecom Services, Inc., one of our subsidiaries, and Potomac Capital Investment Corporation ("PCI"), a wholly-owned subsidiary of Potomac Electric Power Company, formed a joint venture to construct, own, lease, operate and market a communications network to provide voice, video, data and other communications services to residential and commercial customers in the greater Washington, D.C., Virginia and Maryland area. Starpower is an unregulated limited liability company with a perpetual term. We own 50% of the equity interest in Starpower and Pepco Communications owns the remaining 50% interest. Starpower is reflected in our financial statements under the equity method of accounting.

#### *Miscellaneous Facilities Agreements*

We have also entered into agreements which have helped us accelerate network development, including fiber agreements entered into with MFS/WorldCom. MFS/WorldCom owns or has the right to use certain fiber optic network facilities in the Boston, Massachusetts and New York City markets. Under the fiber agreements, MFS/WorldCom agreed to construct and provide extensions connecting the fiber optic facilities to buildings we designated. We are also able to use certain dedicated fibers in those facilities, except that we may not use the facilities to deliver telephone services to commercial customers.

We have also entered into joint construction agreements with Level 3. The agreements will allow us to deploy additional networks in Boston and New York faster and at a lower cost. We also have entered into a letter of intent with Level 3 for Level 3 to provide us with cross-country capacity to allow our customers to connect to major Internet connection points in the United States. This gives us the ability to negotiate peering agreements that will allow the exchange of traffic as a Tier I operator.

In June 1998, we entered into an agreement with Qwest Communications for Qwest to provide us with capacity in its regional backbone of fiber lines to connect to our local networks from Boston to Washington, D.C.

In December 1999 we announced the approval of an agreement with SKANSKA USA, Inc. ("SKANSKA"). Under the contract SKANSKA will initially provide management services to include construction oversight for the installation of the cable television, telephony and data communications' infrastructure in many of our current and targeted markets. Stuart E. Graham, President of SKANSKA, is a member of the Board of Directors of RCN. A competitive bidding process was conducted prior to such agreement. We believe that the agreement has been reached on terms no less favorable than could have been obtained in any arms length negotiation.



## Recent Transactions

In August 1999, we acquired Direct Network Access, Ltd. ("DNAI"), one of the Bay Area's largest independent ISP. We acquired DNAI for approximately \$3.4 million in cash and shares of our common stock with a fair value at the time of issuance of approximately \$6.8 million.

In July 1999, we acquired Brainstorm Networks, Inc. ("Brainstorm"), a leading independent ISP that provides dedicated and DSL services. We purchased Brainstorm for approximately \$2.9 million in cash and shares of our common stock with a fair value at the time of issuance of approximately \$11.6 million.

In April 1999, we acquired a 47.5% ownership interest in JuniorNet Corporation ("JuniorNet"). We purchased the ownership interest for approximately \$47 million in cash. Concurrent with that transaction, JuniorNet purchased our Lancit Media subsidiary ("Lancit") for approximately \$25 million in cash. We acquired Lancit in June 1998 for approximately \$0.4 million in cash and shares of our common stock with a fair value at the time of issuance of approximately \$7.4 million. In February 2000, We made a \$5 million loan to Juniomet in the form of a convertible bridge loan.

We have entered into a definitive agreement with respect to the acquisition of 21st Century Telecom Group, Inc. ("21st Century"). 21st Century is an integrated, facilities-based communications company, which seeks to be the first provider of bundled voice, video and high-speed Internet and data services in selected midwestern markets beginning in Chicago.

## Significant Private Investments

In October 1999, Vulcan Ventures Incorporated ("Vulcan"), the investment organization of Paul G. Allen, agreed to make a \$1.65 billion investment in our company. The investment, which was completed on February 28, 2000, is in the form of mandatorily convertible cumulative preferred stock (the "Preferred Stock"), which will be converted into Common Stock, par value \$1.00 per share ("Common Stock"), no later than seven years after it is issued. Vulcan has purchased 1,650,000 shares of the Preferred Stock. The Preferred Stock has a liquidation preference of \$1,000 per share and is convertible into Common Stock at a price of \$62 per share.

In connection with the investment, Vulcan will generally be authorized to appoint two members to our Board of Directors. On February 28, Vulcan appointed William D. Savoy, President of Vulcan and Edward S. Harris, Investment Analyst with Vulcan. The Preferred Stock will automatically be converted to Common Stock or Class B Stock seven years after the transaction closes, if not previously called or converted. The Preferred Stock has a dividend rate of 7% per annum. All dividends will be paid in additional shares of Preferred Stock.

On April 7, 1999, Hicks, Muse, Tate & Furst, through Hicks Muse Fund IV purchased 250,000 shares of Series A Preferred Stock, par value \$1 per share, for gross proceeds of \$250,000. The Series A Preferred Stock is cumulative and has an annual dividend rate of 7% payable quarterly in cash or additional shares of Series A Preferred Stock and has a initial conversion price of \$39.00 per share. The Series A Preferred Stock is convertible into common stock at any time. The Series A Preferred Stock is subject to a mandatory redemption on March 31, 2014 at \$1,000 per share, plus accrued and unpaid dividends, but may be called by the Company after four years. At December 31, 1999 we paid dividends in the amount of \$13,053 in the form of additional shares of Series A Preferred Stock. At December 31, 1999 the number of common shares that would be issued upon conversion of the Series A Preferred Stock was 6,744,949. We incurred \$10,000 of issuance cost in connection with the sale of the Series A Preferred Stock.

## International

As of July 31, 1999, we executed on a pledge of an 8.96% equity interest in Megacable, the second largest cable television provider in Mexico, made by Mazon Corporativo, S.A. de C.V. ("Mazon") to collateralize Mazon's indebtedness to us. As a result, the indebtedness was cancelled, and our ownership interest in Megacable increased to 48.96%. Megacable owns 26 wireline cable systems in Mexico, principally on the Pacific and Gulf coasts and including Guadalajara, the second largest city in Mexico; Hermosillo, the largest city in the state of Sonora; and Veracruz, the largest city in the state of Veracruz. At December 31, 1999, their wireline systems passed approximately 902,000 homes and served approximately 299,000 subscribers. Megacable had revenues of \$52.2 million and \$37.5 million for the years ended December 31, 1999 and 1998, respectively.

Additionally, Megacable presently holds a 99% interest in Megacable Comunicaciones de Mexico S.A. ("MCM"). MCM has received a license from the Mexican government to allow it to build a fiber optic network in Mexico City, Monterrey and Guadalajara. MCM intends to use this network to provide local voice and high-speed data service in these cities, principally to commercial customers in Mexico City.

## Competition

### Overview

We compete with a wide range of service providers for each of our services. Virtually all markets for voice and video services are extremely competitive, and we expect that competition will intensify in the future. We face significant competition in each of the markets in which we offer voice and video programming services. Our competitors are often larger, better-financed incumbent local telephone carriers and cable companies with better access to capital resources, and many have historically dominated their local telephone and cable television markets. These incumbents presently have numerous advantages as a result of their historic monopolistic control of their respective markets, economies of scale and scope and control of limited conduit and pole space. They also have well-established customer and vendor relationships. However, we believe that most existing and potential competitors will, at least initially, offer narrower services over limited delivery platforms compared to the wide range of voice, video and data services that we provide over our fiber-based networks. This gives us an opportunity to achieve important market penetration.

We compete with the incumbent Local exchange carriers ("LEC's") for the provision of local telephone services, as well as with alternative service providers including CLECs. Cable operators are also entering the local exchange market in some locations. Other sources of competitive local and long distance telephone services include: Commercial mobile radio services providers, including cellular carriers (such as Bell Atlantic Mobile Services); personal communications services carriers such as Sprint PCS; and enhanced specialized mobile radio services providers (such as NexTel).

We face, and expect to continue to face, significant competition for long distance telephone services from the inter-exchange carriers ("IXCs"), including AT&T, Sprint and MCI WorldCom, which account for the majority of all U.S. long distance revenue. The major long distance service providers benefit from established market share and from established trade names through nationwide advertising. However, we regard our long-distance service as a complementary service rather than a principal source of revenue. Certain IXCs, including AT&T, MCI WorldCom and Sprint, have also announced their intention to offer local services in major U.S. markets using their existing infrastructure in combination with resale of incumbent LEC service, lease of unbundled local loops or other providers' services. Internet-based telephony, a potential competitor for low cost telephone service, is also developing and the Company is also pursuing this technology.

All of our video services face competition from alternative methods of receiving and distributing television signals and from other sources of news, information and entertainment. Other sources include off-air television broadcast programming, newspapers, movie theaters, live sporting events, interactive online computer services and home video products, including videotape cassette recorders. Alternative video distribution technologies include traditional cable networks, wireless local video distribution technologies, and home satellite dish ("HSD") earth stations. Home satellite systems enable individual households to receive many of the satellite-delivered program services formerly available only to cable subscribers. The Cable Television Consumer Protection and Competition Act of 1992 (the "1992 Act") contains provisions, which the FCC has implemented with regulations, to enhance the ability of cable competitors to purchase and make available to HSD owners certain satellite-delivered cable programming at competitive costs. We face additional competition from private satellite master antenna television ("SMATV") systems that serve condominiums, apartment and office complexes and private residential developments. The FCC and Congress have adopted policies providing a more favorable operating environment for new and existing technologies that compete, or may compete, with our various video distribution systems. These technologies include, among others, Direct Broadcast Satellite ("DBS") service whereby signals are transmitted by satellite to receiving facilities located on customer premises. We expect that our video programming services will face growing competition from current and new DBS service providers. The FCC has recently determined that DBS is the fastest-growing competitor to franchised cable operations. We also compete with wireless program distribution services such as Multi-Channel Multi-Point Distribution Service which use low-power microwave frequencies to transmit video programming over-the-air to subscribers.

The Internet access market is extremely competitive and highly fragmented. Competition in this market is expected to intensify. Our current and prospective competitors include established online services; local, regional and national ISPs; national and international telecommunications companies including Regional Bell Operating Companies ("RBOCs") such as Bell Atlantic; and affiliates of incumbent cable providers. Increased competition may create downward pressure on the pricing of and margins from Internet access services.

We also compete with companies offering a combination of the services above, such as companies that would result from the merger of Time Warner and America On-line and the merger of AT&T and Media One.

Other new technologies, including Internet-based services, may compete with services that we can offer. Advances in communications technology as well as changes in the marketplace and the regulatory and legislative environment are constantly occurring. Thus, we cannot predict the effect that ongoing or future developments might have on the voice, video and data industries or on our operations or financial condition.

We believe that among the existing competitors, the incumbent LECs, incumbent cable providers and the CLECs are most of our competitors in the delivery of "last mile" connections for voice and video services.

Voice and Video Services  
Incumbent LECs

In each of our target markets for advanced fiber optic networks, we face, and expect to continue to face, significant competition from the incumbent LECs. The incumbent LECs include Bell Atlantic in the Northeast Corridor, and Pacific Bell in California, both of which currently dominate their local telephone markets. We compete with the incumbent LECs in our markets for local exchange services on the basis of product offerings, including the ability to offer bundled voice and video service, reliability, state-of-the-art technology and superior customer service, as well as price. We believe that our advanced fiber optic networks provide superior technology for delivering high-speed, high-capacity voice, video and data services compared to the incumbent LECs' primarily copper wire based networks. However, the incumbent LECs have long-standing relationships with their customers. They have also begun to expand the amount of fiber facilities in their networks, offer broadband digital transmission services and retail Internet access, and prepare to re-enter the long distance telephone service market.

The pending merger between Bell Atlantic and GTE Corporation may enhance the combined entity's ability to compete with us in the Northeast corridor markets. The merger between SBC and Ameritech may also increase competitive pressures in the Northeast corridor if SBC, which already owns a Connecticut incumbent LEC and several wireless franchises in this region, continues to pursue a nationwide strategy.

Under the Telecommunications Act of 1996 (the "1996 Act"), and ensuing federal and state regulatory initiatives, barriers to local exchange competition are being slowly removed. The introduction of such competition, however, also establishes the predicate for the RBOCs, such as Bell Atlantic, to provide in-region interexchange long distance services. The RBOCs are currently allowed to offer "incidental" long distance service in-region and to offer out-of-region long distance service. Once the RBOCs are allowed to offer in-region long distance services, they will also be in a position to offer single source local and long distance service similar to what we offer and what is proposed by the three largest IXCs: AT&T, MCI WorldCom and Sprint. We expect that the increased competition made possible by regulatory reform will result in certain pricing and margin pressures in the telecommunications services business.

We have sought, and will continue to seek, to provide a full range of local voice services which compete with incumbent LECs in our service areas. We expect that competition for local telephone services will be based primarily on quality, capacity and reliability of network facilities, customer service, response to customer needs, service features and price, and will not be based on any proprietary technology. Our new fiber optic networks, employ dual backbone architecture and advanced technology; therefore, we may have capital cost and service quality advantages over some of the networks of the incumbent LECs. We may also have a competitive advantage because we are able to deliver a bundled voice and video service.

The 1996 Act permits the incumbent LECs and others with which we compete to provide a wide variety of video services directly to subscribers. Various LECs currently are providing video services within and outside their telephone service areas through a variety of distribution methods, including both the deployment of broadband wire facilities and the use of wireless transmission facilities. We cannot predict the likelihood of success of video service ventures by LECs or the impact such competitive ventures may have on us. Some LECs, including Bell Atlantic, also offer Internet access services that compete with RCN.com services.

### Incumbent Cable Television Service Providers

Certain of our video service businesses compete with incumbent wireline cable companies in their respective service areas. In particular, our advanced fiber optic networks compete for cable subscribers with the major wireline cable operators in our markets, such as Time-Warner Cable in New York City, Cablevision in Boston and TCI in Washington, D.C. and San Francisco. Our wireless video service in New York City competes primarily with Time-Warner Cable. We believe that the expanded capacity and fiber-to-node architecture of our advanced fiber optic networks make us better equipped to provide high-capacity communications services than traditional coaxial cable based networks using "tree and branch" architecture. Our Lehigh Valley, Pennsylvania hybrid fiber/coaxial cable television system competes with an alternate service provider, Service Electric, which also holds a franchise for the relevant service area.

Cable television systems generally operate pursuant to franchises granted on a non-exclusive basis, and the 1992 Act prohibits franchising authorities from unreasonably denying requests for additional franchises and permits franchising authorities to operate cable systems. Therefore, well-financed businesses from outside the cable industry, such as the public utilities that own certain of the conduits or poles which carry cable, may become competitors for franchises or providers of competing services. Telephone companies or others may also enter the video distribution market by becoming open video service operators as we have done in several markets, pursuant to Section 653 of the Communications Act. No local franchise is required for the provision of such service, but see regulation of Video services below.

### CLECs and Other Competitors

We also face, and expect to continue to face, competition from other potential competitors in certain of our geographic markets. Other CLECs, such as subsidiaries of AT&T and MCI WorldCom, compete for local telephone services, although they have, to date, focused primarily on the market for commercial customers rather than residential customers. In addition, potential competitors capable of offering private line and special access services also include other smaller long distance carriers, cable television companies, electric utilities, microwave carriers, wireless telephone system operators and private networks built by large end-users, including Winstar, Dualstar and New Vision. However, we believe that, at least initially, we are relatively unique in our markets in offering bundled voice, video and data services primarily to customers in residential areas over our own advanced fiber optic network.

### Internet Services

The Internet access market is extremely competitive and highly fragmented. No significant barriers to entry exist and, accordingly, competition in this market is expected to intensify. Our current and prospective competitors include many large companies with substantially greater market presence and financial and other resources. RCN.com competes directly or indirectly with:

- o established online services, such as America Online, the Microsoft Network and Prodigy;
- o local, regional and national ISPs such as PSINet, EarthLink, Mindspring and Rocky Mountain Internet;
- o the Internet services of national and international telecommunications companies, such as AT&T, GTE, MCI WorldCom and Cable & Wireless;
- o Internet access (including high speed digital subscriber line service) offered by RBOCs such as Bell Atlantic; and
- o online services offered by incumbent cable providers, such as At Home and Roadrunner.

Bell Atlantic has recently asked the FCC to authorize it to build a regional high-speed network, which would serve as an Internet backbone, and to exempt this network from pricing and other regulatory restrictions. The network would span the states from Maine to Virginia. Internet access competition is likely to increase as large diversified telecommunications and media companies acquire ISPs and as ISPs consolidate into larger, more competitive companies. For example, AT&T has completed the acquisitions of TCI's cable television networks, which gives it a significant ownership interest in At Home, an ISP. Diversified competitors may bundle other services and products with Internet connectivity services, potentially placing us at a competitive disadvantage. In addition, competitors may create downward pressure on the pricing of and margins from Internet access services. Competition could also impact our ability to participate in transit agreements and peering arrangements, which could, in turn, adversely effect the speed of service that we can provide to our customers.

Other new technologies may become competitive with our services. A provider of Limited Multi Distribution Systems ("LMDS") recently began offering wireless Internet and video programming services in New York City and has announced plans to offer telephone service in the future. Advances in communications technology as well as changes in the marketplace and the regulatory and legislative environment are constantly occurring. In addition, a continuing trend toward business combinations and alliances in the telecommunications industry may also create significant new competitors. We cannot predict the effect that competition from developing and future technologies or from future competitors will have on our operations or financial condition.

## Regulation

Our telephone and video programming transmission services are subject to federal, state and local government regulation. The 1996 Act introduced widespread changes in the regulation of the communications industry, including the local telephone, long distance telephone, data services, and television entertainment segments. The 1996 Act was intended to promote competition and decrease regulation of these segments of the industry. The law delegates to both the FCC and the states broad regulatory and administrative authority to implement the 1996 Act.

### Telecommunications Act of 1996

The 1996 Act eliminates many of the pre-existing legal barriers to competition in the telephone and video programming communications businesses. The Act also preempts many of the state barriers to local telephone service competition that previously existed in state and local laws and regulations and sets basic standards for relationships between telecommunications providers.

The 1996 Act removes barriers to entry in the local exchange telephone market by preempting state and local laws that restrict competition and by requiring LECs to provide nondiscriminatory access and interconnection to potential competitors, such as cable operators, wireless telecommunications providers, and long distance companies. In addition, the 1996 Act provides relief from the earnings restrictions and price controls that have governed the local telephone business for many years. The 1996 Act will also, once certain thresholds are met, allow incumbent RBOCs to enter the long distance market within their own local service regions.

Regulations promulgated by the FCC under the 1996 Act require LECs to open their telephone networks to competition by providing competitors interconnection, access to unbundled network elements and retail services at wholesale rates. As a result of these changes, companies such as ours are now able to interconnect with the incumbent LECs in order to provide local exchange services. Numerous parties appealed certain aspects of these regulations, and implementation of several provisions of the rules was delayed while the courts considered these appeals. On January 25, 1999, the Supreme Court issued an opinion confirming the FCC's authority to issue regulations implementing the pricing and other provisions of the 1996 Act and reinstating most of the challenged rules. While the Supreme Court confirmed that the FCC has authority to issue rules implementing the 1996 Act, particular rules still may be challenged in future court proceedings. Future regulatory proceedings and court appeals may create delay and uncertainty in effectuating the interconnection and local competition provisions of the 1996 Act. Recent decisions by the FCC, including a proceeding resulting from the Supreme Court decision described above, have reaffirmed the incumbent LECs' obligation to unbundle most elements of their networks, and have expanded these obligations in some respects. Because we are building our own networks rather than relying on the incumbent LECs' facilities, these rulings may benefit us less than they do some of our competitors. However, we do require interconnection with the incumbent LECs for a variety of purposes, and regulatory actions have generally facilitated this interconnection.

We have entered into interconnection agreements with Bell Atlantic, Pacific Bell and other incumbent LECs serving our target market areas. Some of these agreements have expired or will expire shortly. As a general matter, our agreements provide for service to continue without interruption while a new agreement is negotiated. Most of the agreements also provide for amendments in the event of changes in the law, such as the regulatory and court decisions described above. We cannot assure you, however, that we will be able to obtain or enforce future interconnection agreements, or obtain renewal of existing agreements, on acceptable terms.

The 1996 Act establishes certain conditions before RBOCs are allowed to offer interLATA long distance service to customers within their local service regions. These conditions include 14 "checklist" requirements designed to open the RBOC networks to competitors. To date, the only RBOC that has received FCC authorization to provide in-region long distance service is Bell Atlantic for New York, although other applications may be approved in the future. If an RBOC is authorized to provide in-region long distance service in one or more states, the RBOC may be able to offer "one-stop shopping" services that compete with our service offerings. See "Business-Competition". In addition, the RBOC will lose the incentive it now has to rapidly implement the interconnection provisions of the 1996 Act in order to obtain in-region authority, although the RBOC will still be subject to a legal obligation to comply with those provisions.

The 1996 Act also makes far-reaching changes in the regulation of video programming transmission services. These include changes to the regulations applicable to video operators, the elimination of restrictions on telephone company entry into the video business, and the establishment of a new OVS regulatory structure for telephone companies and others. Under the 1996 Act and implementing rules adopted by the FCC, local telephone companies, including both incumbent LECs such as Bell Atlantic, and CLECs such as RCN, may provide service as traditional cable television operators subject to municipal cable television franchises, or they may choose to provide their programming over open video systems. Although OVS operators are not required to secure local franchises by federal law, local franchising authorities may legally require such a franchise. To date, however, none have done so. OVS operators must make available a portion of their channel capacity for use by unaffiliated program distributors and must satisfy certain other requirements, including providing capacity for public, educational and government channels, and paying a gross receipts fee equal to the franchise fee paid by the incumbent cable television operator. We are one of the first CLECs to provide television programming over an advanced fiber optic network under the OVS regulations implemented by the FCC under the 1996 Act. As discussed below, we are currently providing OVS service in certain suburbs of Boston, in the City of New York, Washington, D.C. and in a limited number of smaller communities. We are also negotiating similar agreements in Northern New Jersey, Philadelphia and surrounding communities, and communities surrounding San Francisco. Starpower is negotiating similar OVS agreements and local franchises in communities surrounding Washington D.C.

#### Regulation of Voice Services

Our voice business is subject to regulation by the FCC at the federal level for interstate telephone services (i.e., those that originate in one state and terminate in a different state). State regulatory commissions have jurisdiction over intrastate communications (i.e., those that originate and terminate in the same state).

**State Regulation of Intrastate Local and Long Distance Telephone Services.** Our intrastate telephone services are regulated by the public service commissions or comparable agencies of the various states in which we offer these services. Our subsidiaries or affiliates have received authority to offer intrastate telephone services, including local exchange service, in substantially all of the states in our target market areas, and have applications for such authorization pending in several additional states. We also have authority to provide in-state long distance services in all states except Alaska and Hawaii. To date, none of our applications for state authorizations has been rejected.

**FCC Regulation of Interstate and International Telephone Services.** We provide domestic interstate telephone services nationwide under tariffs on file at the FCC. We have been authorized by the FCC under Section 214 of the 1996 Act to offer worldwide international services as well.



Local Regulation of Telephone Services. Municipalities also regulate limited aspects of our voice business by, for example, imposing various zoning requirements. In some instances, they require telecommunications licenses, franchise agreements and/or installation permits for access to local streets and rights-of-way. In New York City, for example, we will be required to obtain a telephone franchise in order to provide voice services using our advanced fiber optic network facilities located in the streets of New York City, although services may be provided over certain leased or resold facilities while we wait to receive a franchise.

#### Regulation of Video Services

Open Video Systems. At various times between February 1997 and December 1999, our subsidiaries and affiliates have been certified by the FCC to operate OVS networks in New York City, Boston, Washington, D.C., Philadelphia, Los Angeles, Phoenix, Portland, Seattle, and San Francisco, and communities surrounding each of these cities, Cook County, Illinois and in the Northern New Jersey area. Initiation of OVS services is subject to completion of an open enrollment period for non-affiliated video programmers to seek capacity on the systems and after negotiation of certain agreements with local governments. The initial open enrollment period for each of these systems has expired, except for the Northern New Jersey system, Philadelphia, Los Angeles, Portland, Seattle, Cook County and Phoenix where the open enrollment period has not yet begun. We executed an agreement with the City of Boston on June 2, 1997, and initiated OVS service in the City on that day. Under our agreement with the City of Boston, we were required to pay a fee to the City equal to 5% of video revenues. We have entered into similar OVS agreements or are in the process of negotiating agreements with certain other Boston-area municipalities, either to offer OVS services or franchised cable television services. In July of 1999 the OVS Agreement with Boston was terminated by mutual consent and a franchise agreement was substituted therefore. We entered into an agreement with the City of New York on December 29, 1997 and have initiated OVS service in the Borough of Manhattan. RCN also provides video distribution service in Manhattan and a portion of the Bronx using microwave facilities and antennas located at multiple dwelling units. On July 10, 1998, we supplemented our agreement with the City of New York to include all five boroughs. On October 26, 1998, Starpower entered into an agreement with the District of Columbia and initiated OVS service in the District in the last quarter of 1998. Starpower has entered into similar agreements or is in the process of negotiating agreements with numerous suburban communities near Washington, D.C., to offer either OVS services or franchised cable television services.

In areas where we offer video programming services as an OVS operator, we are required to make any "open capacity" on the system available to unaffiliated Video Program Providers ("VPPs"). The commissions rules permit us to retain up to one-third of the system capacity for our own (or affiliate's) use. Under the OVS regulations, during the initial open enrollment period we must offer at least two-thirds of our capacity to unaffiliated parties, if demand for such capacity exists during the open enrollment period. In certain areas, at the request of local officials, we are in discussions to explore the feasibility of obtaining a cable franchise instead of an OVS agreement. We will consider providing RCN video service under franchise agreements rather than OVS certification, if franchise agreements are preferred by the local authorities and can be obtained on acceptable terms and conditions. We will consider the relative benefits of OVS certification versus local franchise agreements, including the possible imposition of build out requirements, before making any decisions.

In a decision released in January of 1999, the U.S. Court of Appeals for the Fifth Circuit approved some portions of the FCC's OVS rules but struck down other portions. Although a number of the Court's rulings are favorable to OVS operators, others could have an adverse impact on our OVS operations and planning. The Court's most significant decision was to strike down the FCC's rule preempting local authority to franchise OVS operators. The FCC's rules had set forth a relatively simple procedure at the FCC for rapid certification of each OVS system on a regional basis and permitted local authorities to regulate OVS only as to rights-of-way administration and in other minor respects. One of the principal advantages of OVS as structured by Congress and by the FCC was to eliminate the time, expense, and uncertainty generally required to secure a local franchise. The Court's action allowing local governments to require area-by-area franchising may significantly reduce the advantage of OVS operation as compared with traditional franchising and delay achieving agreements with local governments. To date, however, no local franchising authority has insisted on franchising OVS systems, although some have considered doing so. However, in many instances RCN, at the insistence of local authorities, has been negotiating franchise agreements in lieu of OVS agreements and agreeing to provisions in OVS right-of-way agreements which to some extent erode the differences between the two modes of operation. Accordingly, while the ruling is disadvantageous to us, we expect to continue to expand our video service offerings.

The FCC's rules require OVS operators to make their facilities available to video program providers on a non-discriminatory basis, with certain exceptions. One exception is that competing in-region cable operators are not entitled to become video program providers on an OVS except in certain limited circumstances. Time Warner Cable Co., which then operated franchised cable systems in many suburban Boston communities included within our OVS certification, also petitioned the FCC for an order compelling us to release certain OVS system data so that it allegedly could analyze the possibility of being a VPP on RCN's OVS. Time Warner was not then competing with any RCN-provided OVS service and restricted its request to communities where it is not the franchised cable operator. RCN denied the request on the ground that the Time Warner should be considered ineligible under the FCC's rules. Time Warner filed an OVS complaint against RCN and also sought FCC action to impose fines or cancel our OVS authority. The Cable Services Bureau ruled that Time Warner was an eligible user in areas where no service overlap existed or was imminent, partially granted the data request, and partially denied it, but found too little evidence to justify further exploration of our good faith in implementing OVS authority. We sought partial reconsideration of the Bureau's order. Time Warner filed a similar complaint against us in New York City where we compete with it for video distribution business in Manhattan. The FCC's Cable Services Bureau partially granted Time Warner's complaint, and partially denied it, relying on its prior decision in the Time Warner complaint in the Boston area. We sought partial reconsideration of both decisions.

The FCC issued a consolidated opinion in which it rejected the analysis underlying the Cable Services Bureau's conclusions with respect to Time Warner's eligibility to use the OVS system and in lieu thereof reinterpreted the relevant rule by substituting a newly-formulated test of eligibility based on whether the in-region cable competitor is franchised within the "technically integrated service area" of the OVS certificate holder. The Commission also confirmed the Cable Services Bureau's rulings on the scope of the OVS data which must be disclosed to Time Warner, and directed RCN to file supplemental data with the Cable Services Bureau concerning the Commission's new interpretation of the relevant rule. The Commission indicated that upon the submission of such data the Cable Services Bureau was to determine whether Time Warner was eligible for the OVS data it had been seeking from RCN.

RCN is seeking review of the FCC's decision in the U.S. Court of Appeals for the D.C. Circuit, alleging that the Commission's interpretation of the rule governing the eligibility of an in-region competitor to be a VPP was contrary to law. Time Warner sought reconsideration of the decision at the FCC. Time Warner also sought intervention in the Court of Appeals and the FCC has asked the Court to hold the case in abeyance pending the resolution of Time Warner's request for reconsideration. The Court granted both motions. RCN filed the supplemental service area data with the Cable Services Bureau as required by the Commission's decision for the Boston and New York markets but sought a stay of the obligation to make such filings in other markets where RCN has been certificated and has already filed certain so-called "notices of intent." The Cable Services Bureau denied RCN's request for stay, and RCN thereupon filed the supplemental data for all relevant OVS markets. RCN has sought confidential treatment from the Commission of those portions of the supplemental data which were not publicly available already, contending that it would be seriously damaged competitively if it were required to provide such data to its in-region competitor. RCN contended also that the provision of such data to Time Warner (or any in-region cable competitor in other markets) prior to the Court's consideration of RCN's appeal would deny RCN its due process rights to have the necessity for such disclosure of competitively sensitive data adjudicated by the Court of Appeals. The Commission has not yet ruled on these requests for confidential treatment.

On February 10, 2000 Time Warner renewed its request for OVS data from RCN for certain suburban communities in the Boston metropolitan area, alleging that it had sold its cable properties within RCN's certified OVS area to MediaOne and hence was no longer an in-region cable competitor. RCN declined to provide such data, noting that Time Warner had certain affiliations with MediaOne through the proposed acquisition of MediaOne by AT&T and that Time Warner had not indicated whether it had any residual contractual rights, or data sharing obligations with MediaOne or AT&T. On March 14, 2000, Time Warner filed an "Emergency Petition to Enforce Commission Order and Impose Forfeiture" renewing earlier allegations that RCN was not adhering to certain of the OVS rules and was not operating a truly "open" OVS system. Time Warner sought an order compelling RCN to provide the OVS data to Time Warner, and for the imposition of forfeitures on RCN for allegedly failing to comply with Commission orders. RCN is opposing the Emergency Petition and the Commission has not yet acted on it.

Two additional cable company OVS access complaints have been filed against Starpower, seeking data and a determination of eligibility for carriage on the metropolitan Washington, D.C. OVS system. As in the prior complaints, they challenge our status as an OVS operator and seek to revoke our OVS authority. These complaints were filed by Media General Cable of Fairfax, Inc., and Media General Cable of Fredericksburg, Inc. Both claimed to be seeking system data for areas in which they do not provide franchised service. Starpower declined to provide system data to either complainant. Media General has also sought to initiate discovery against Starpower. The Cable Services Bureau, citing its prior decision in Boston and New York, granted the Media General request. Starpower sought reconsideration which is still pending. The complaining Media General companies have since been acquired by Cox Cable, Inc.

Cable industry representatives have opposed or commented adversely on two other RCN OVS initiatives. In respect to our application for OVS authority in the San Francisco area, the California Cable Television Association filed an opposition, alleging that we were misusing the OVS rules to compete unfairly against franchised cable operators. The Pennsylvania Cable & Telecommunications Association filed comments on our OVS application for OVS authority in the Philadelphia region, making similar allegations but not formally opposing the application. The Cable Services Bureau granted both of our applications, indicating that our applications were consistent with the rules and that the opposing parties had not provided sufficient evidence to justify initiating any regulatory action against us. There is language in each of these Cable Bureau determinations involving our implementation of the OVS concept which leave open the possibility for adverse parties to challenge our status as an OVS operator. We believe that we are operating in strict conformity with all applicable provisions of the law and will continue to defend our OVS roll-outs against what we believe are anti-competitive requests for data or carriage by competing in-region cable operators. However, we cannot assure you that the FCC or the Court of Appeals will resolve the pending OVS complaints in our favor. If the FCC were to grant any such complaints and as a result we were obliged to share system data with our local competitors, we would be forced to reassess the desirability of continuing to operate in certain markets as an OVS operator as compared with seeking traditional cable franchises. We do not believe that abandoning our OVS certifications under such circumstances would materially adversely affect our video distribution activities.

As in the case of traditional franchised cable systems, OVS operators must in virtually all locations have access to public rights-of-way for their distribution plant. In a number of jurisdictions local authorities have attempted to impose rights-of-way fees on us which we believe are in violation of federal law. A number of FCC and judicial decisions have addressed the issues posed by the imposition of rights-of-way fees on CLECs and on video distributors. To date the state of the law is uncertain and may remain so for some time. The obligation to pay local rights-of-way fees which are excessive or discriminatory could have adverse effects on our business activities. See "Legal proceedings" below. The incumbent cable operator in Boston, MA, Cablevision of Boston, Inc., filed suit in 1999 in U.S. District Court in Boston against the City of Boston, RCN-BECOCOM, RCN, BECOCOM and others, alleging that the City had followed a discriminatory policy in administering access to public rights-of-way for the installation and use of underground conduit and that the private defendants had participated in an effort to unlawfully construct and use underground conduit. Cablevision claimed that the defendants were in violation of the 1996 Act and Massachusetts state law, and sought a preliminary injunction. RCN and the other defendants denied participating in any unlawful activity. The Court denied the preliminary injunction. The First Circuit Court of Appeals affirmed and thereafter Cablevision withdrew the suit.

Access issues have also arisen in a proceeding before the Massachusetts Department of Telecommunications and Energy (the "MDTE"). In 1997, the MDTE opened an investigation into Boston Edison Company's compliance with a MDTE order in 1993 that permitted Boston Edison to invest up to \$45 million in its unregulated subsidiary Boston Edison Technology Group for three limited purposes. RCN-BECOCOM intervened in the current proceeding, as did Cablevision Systems Corporation and the New England Cable Television Association, Inc., along with the Massachusetts Attorney General's office. Hearings began in December 1998 and are still proceeding. The intervenors, in particular Cablevision, have advocated that if the MDTE finds that Boston Edison's investment in RCN-BECOCOM violated the 1993 Order then Boston Edison should be forced to divest itself of its interest in RCN-BECOCOM, RCN-BECOCOM should be subject to the same terms and conditions as other cable television providers who seek to attach their facilities to Boston Edison facilities, and installed RCN-BECOCOM cable and fiber-optic facilities should be relocated. Boston Edison is vigorously defending the propriety of its compliance with the MDTE's 1993 Order, and its investment in RCN-BECOCOM. RCN cannot assure you that the MDTE will not determine that Boston Edison violated the MDTE's 1993 Order nor can RCN assure you as to the nature of any remedy that the MDTE may determine to be appropriate including those proposed remedies which are equitable in nature. RCN is participating in the proceeding and plans to take such action as it deems appropriate to protect its rights.

**Wireless Video Services.** Our 18 GHz wireless video services in New York City are distributed using microwave facilities. We are currently using one microwave path on the basis of a conditional license. We anticipate our pending application for this path will be granted soon by the FCC. However, our failure to obtain this license might adversely affect our wireless video operations in New York City.

We cannot assure you that we will be able to obtain or retain all necessary authorizations needed to construct advanced fiber optic network facilities, to convert our wireless video subscribers to an advanced fiber optic network or to offer wireless video services under our own FCC licenses.

Hybrid Fiber/Coaxial Cable. Our hybrid fiber/coaxial cable systems are subject to regulation under the 1992 Act. The 1992 Act regulates rates for cable services in communities that are not subject to "effective competition," certain programming requirements, and broadcast signal carriage requirements that allow local commercial television broadcast stations to require a cable system to carry the station. Local commercial television broadcast stations may elect once every three years to require a cable system to carry the station ("must-carry"), subject to certain exceptions, or to withhold consent and negotiate the terms of carriage ("retransmission consent"). A cable system generally is required to devote up to one-third of its activated channel capacity for the carriage of local commercial television stations whether under the mandatory carriage or retransmission consent requirements of the 1992 Act. Local non-commercial television stations are also given mandatory carriage rights. The FCC recently issued rules establishing standards for digital television ("DTV"). The FCC's rules require television stations to simulcast their existing television signals ("NTSC") and DTV signals for a period of years. During this simulcast period, it is unclear whether must-carry rules will apply to DTV signals. The FCC has initiated a rule making proceeding seeking comment on the carriage of broadcast DTV signals by cable and OVS operators during the transitional period to full digital broadcasting. The FCC's proceeding addresses the need for the digital systems to be compatible, seeks comment on possible changes to the mandatory carriage rules, and explores the impact carriage of DTV signals may have on other FCC rules. The cable industry has generally opposed many of the FCC's proposals, on the grounds that they constitute excessively burdensome obligations on the industry. The Communications Act permits franchising authorities to require cable operators to set aside certain channels for public, educational and governmental access programming. Cable systems with 36 or more channels must designate a portion of their channel capacity for commercial leased access by third parties to provide programming that may compete with services offered by the cable operator.

Because a cable communications system uses local streets and rights-of-way, such cable systems are generally subject to state and local regulation, typically imposed through the franchising process. The terms and conditions of state or local government franchises vary materially from jurisdiction to jurisdiction. Generally, they contain provisions governing cable service rates, franchise fees, franchise term, system construction and maintenance obligations, customer service standards, franchise renewal, sale or transfer of the franchise, territory of the franchisee and use and occupancy of public streets and types of cable services provided. Local franchising authorities may award one or more franchises within their jurisdictions and prohibit non-grandfathered cable systems from operating without a franchise. The Communications Act also provides that in granting or renewing franchises, local authorities may establish requirements for cable-related facilities and equipment, but not for video programming or information services other than in broad categories. The Communications Act limits franchise fees to 5% of revenues derived from cable operations and permits the cable operator to seek modification of if franchise requirements through the franchise authority or by judicial action changed circumstances warrant.

Our ability to provide franchised cable television services depends largely on our ability to obtain and renew our franchise agreements from local government authorities on generally acceptable terms. We currently have 91 franchise agreements relating to the hybrid fiber/coaxial cable systems in New York (outside New York City), New Jersey and Pennsylvania. These franchises typically contain many conditions, such as time limitations on commencement and completion of construction, conditions of service, including the number of channels, the provision of free service to schools and certain other public institutions, and the maintenance of insurance and indemnity bonds. These franchises provide for the payment of fees to the issuing authorities and generally range from 3% to 5% of revenues. The duration of these outstanding franchises presently varies up to the year 2011. To date, all of our cable franchises have been renewed or extended, generally at or before their stated expirations and on acceptable terms. Approximately 39 of our hybrid fiber/coaxial cable systems' franchises are due for renewal within the next three years. We cannot assure you that we will be able to renew our franchises on acceptable terms. No one franchise accounts for more than 7% of our total revenue. Our five largest franchises account for approximately 27% of our total revenue.

Hybrid fiber/coaxial cable systems are also subject to certain service quality standards and other obligations imposed by the FCC and, where effective competition has not been demonstrated to exist, had been subject to rate regulation by the FCC as well. Our cable television system in Pennsylvania has been operating in a competitive cable environment for almost 30 years, with approximately 80% of the homes passed having access to an alternate cable operator, Service Electric Cable TV. As a result, our Pennsylvania cable system is exempt from many FCC cable television regulations, including rate regulation. Our other cable television systems in New York State and New Jersey had been subject to FCC rate regulation. As required by the 1996 Act, however, all cable programming services were deregulated on March 31, 1999. There has been discussion in Congress about possible legislation to reimpose cable rate regulation. We cannot assure you that legislation will not be adopted. We anticipate that the remaining provisions of the 1992 Act that do not relate to rate regulation, including provisions relating to retransmission consent and customer service standards, will remain in place and may reduce the future operating margins of our hybrid fiber/coaxial cable television businesses as video programming competition develops in our cable television service markets.

The FCC is required to regulate the rates, terms and conditions imposed by utilities. ILEC's and CLEC's for cable systems' and telecommunications providers use of utility pole and conduit space unless state authorities can demonstrate that they adequately regulate pole attachment rates. In the absence of state regulation, the FCC administers pole attachment rates on a formula basis. In some cases, utility companies have increased pole attachment fees for cable systems that have installed fiber optic cables and that are using these cables for the distribution of non-video services. The FCC concluded that, in the absence of state regulation, it can determine whether utility companies have justified their demand for additional rental fees and that the Communications Act does not permit disparate rates based on the type of service provided over the equipment attached to the utility's pole. The 1996 Act modified the prior pole attachment provisions of the Communications Act. It permits providers of telecommunications services to rely upon the protections of the current law and requires that utilities provide cable systems and telecommunications carriers with nondiscriminatory access to any pole, conduit or right-of-way, owned or controlled by the utility if the facility is carrying wires already. The FCC adopted new regulations to govern the charges for pole attachments used by companies providing telecommunications services, including cable operators. These regulations will become effective five years after enactment of the 1996 Act, and any increase in attachment rates resulting from the FCC's new regulations will be phased in in equal annual increments over a period of five years beginning on the effective date of the new FCC regulations. The ultimate outcome of these rulemakings and the ultimate impact of any revised FCC rate formula or of any new pole attachment rate regulations on us or our businesses cannot be determined at this time.

The 1992 Act, the 1996 Act and FCC regulations preclude any cable operator or satellite video programmer affiliated with a cable company, or with a common carrier providing video programming directly to its subscribers, from favoring an affiliated company over competitors. In certain circumstances, these programmers are required to sell their programming to other multichannel video distributors. The provisions limit the ability of program suppliers affiliated with cable companies or with common carriers providing satellite delivered video programming directly to their subscribers to offer exclusive programming arrangements to their affiliates. The FCC's Cable Service Bureau, however, has ruled that, except in limited circumstances, these statutory and regulatory limitations do not apply to programming which is distributed other than by satellite. We are experiencing difficulty in securing access to certain local sports programming in the New York City market, which we consider important to successful competition in that market. RCN brought a formal program access complaint against Cablevision Systems, Inc. over its refusal to provide such programming to RCN. The Cable Services Bureau sustained its traditional view, however, that programming distributed by fiber optic cable was not covered by the program access provisions of the Communications Act, and denied RCN's complaint. RCN believes that the Cable Services Bureau is misreading the law and has sought review by the full Commission of this ruling. The Communications Act also includes provisions concerning horizontal and vertical ownership of cable systems, customer service, subscriber privacy, marketing practices, equal employment opportunity, obscene or indecent programming, regulation of technical standards and equipment compatibility.



In addition to the FCC regulations previously discussed, there are other FCC regulations covering areas such as:

- o equal employment opportunity;
- o syndicated program exclusivity;
- o network program non-duplication;
- o registration of cable systems;
- o maintenance of various records and public inspection files;
- o microwave frequency usage;
- o lockbox availability;
- o sponsorship identification;
- o antenna structure notification;
- o tower marking and lighting;
- o carriage of local sports broadcast programming;
- o application of rules governing political broadcasts;
- o limitations on advertising contained in non-broadcast children's programming;
- o consumer protection and customer service;
- o ownership and access to cable home wiring and home wiring in multiple dwelling units;
- o indecent programming;
- o programmer access to cable systems;
- o programming agreements;
- o technical standards; and
- o consumer electronics equipment compatibility and closed captioning.

The FCC has the authority to enforce its regulations through imposing substantial fines, issuing cease and desist orders and/or imposing other administrative sanctions, such as revoking FCC licenses needed to operate certain transmission facilities often used in connection with cable operations. We have had difficulty gaining access to the video distribution wiring in certain multiple dwelling units in the City of Boston in which Cablevision is the incumbent provider of video services. In some buildings the management will not permit us to install our own distribution wiring and Cablevision has not been willing to permit us to use the existing wiring on some equitable basis when we wish to initiate service to an individual unit previously served by Cablevision. We have sought a ruling from the FCC's Cable Services Bureau that existing FCC inside wiring rules require Cablevision to cooperate with us to make such wiring available to it. The matter is currently pending before the FCC's Cable Services Bureau staff. However, because RCN status in the city of Boston has changed from OVS operator to franchisee, we will be able to use the Massachusetts Mandatory Access law if it is necessary to do so to gain access to these MDUs.

Other bills and administrative proposals pertaining to cable television have previously been introduced in Congress or considered by other governmental bodies over the past several years. There will likely be legislative proposals in the future by Congress and other governmental bodies relating to the regulation of communications services.

Cable television systems are subject to federal compulsory copyright licensing covering the retransmission of television and radio broadcast signals. In exchange for filing certain reports and contributing a percentage of their basic revenues to a federal copyright royalty pool, cable operators can obtain blanket licenses to retransmit the copyrighted material on broadcast signals. Numerous jurisdictions have imposed so-called "open access" requirements for the grant or transfer of a cable franchise and many more are considering doing so. RCN believes its business interests may be served by such open access but is opposed to further regulations or government intervention in regard to such matters.

Responding to pressure principally from direct broadcast satellite ("DBS") companies, Congress passed the Satellite Home Viewer Improvement Act in late fall of 1999. The principal purpose of this legislation, known as "SHVIA" was to amend the copyright law to permit the DBS companies to carry more local broadcast programming in their programming packages (so-called "local-into-local"). At the same time the legislation directed the FCC to develop new regulations concerning retransmission consent and mandatory access. The retransmission consent provision of SHVIA covers all multiple video program distributors as well as DBS providers. The Commission has adopted its retransmission consent rules as required in SHVIA. These new regulations establish an obligation on the part of broadcasters to bargain in good faith and define good faith by reference to certain prohibited bargaining tactics or positions. The regulations also bar exclusive retransmission agreements but do permit broadcasters to enter into varying terms with MVPDs carrying their signal based on normal competitive criteria. To the extent RCN will need to negotiate such *retransmission consent agreements in the future these regulations should help to strength our negotiating position.*

**Other Regulatory Issues.** The data services business, including Internet access, is largely unregulated at this time apart from Federal, state and local laws and regulations applicable to businesses in general. However, we cannot assure you that this business will not become subject to regulatory restraints. Some federal, state, local and foreign governmental organizations are considering a number of legislative and regulatory proposals with respect to Internet user privacy, infringement, pricing, quality of products and services and intellectual property ownership. We are also unsure how existing laws will be applied to the Internet in areas such as property ownership, copyright, trademark, trade secret, obscenity and defamation. Additionally, some jurisdictions have sought to impose taxes and other burdens on providers of data services, and to regulate content provided via the Internet and other information services. We expect that proposals of this nature will continue to be debated in Congress and state legislatures in the future. In addition, although the FCC has on several occasions rejected proposals to impose additional costs on providers of Internet access service and other data services for the use of local exchange telephone network facilities for access to their customers, the FCC or Congress may consider similar proposals in the future. The adoption of new laws or the adaptation of existing laws to the Internet may decrease the growth in the use of the Internet, which could in turn have a material adverse effect on our Internet business.